

D.T.E. 01-52

Petition of Southern Union Company for authorization and approval to issue and distribute up to 2.7 million shares of common stock as a dividend payment to the Company's equity shareholders pursuant to the provisions of G.L. c. 164, §§ 11 and 14.

---

APPEARANCES: Robert J. Keegan, Esq.  
Cheryl M. Kimball, Esq.  
Keegan, Werlin & Pabian  
21 Custom House Street  
Boston, Massachusetts 02110  
FOR: SOUTHERN UNION COMPANY  
Petitioner

Thomas F. Reilly, Attorney General  
By: Wilner Borgella  
Assistant Attorney General  
200 Portland Street  
Boston, Massachusetts 02114  
Intervenor

## I. INTRODUCTION

On May 17, 2001, Southern Union Company (“Southern Union” or “Company”) petitioned the Department of Telecommunications and Energy (“Department”) pursuant to G.L. c. 164, §§ 11 and 14 for authorization and approval to issue and distribute up to 2.7 million shares of common stock as a dividend payment to the Company’s equity shareholders.<sup>1</sup> The Attorney General intervened in the matter under the authority granted him by G.L. c. 12, § 11E. The Department docketed the filing as D.T.E. 01-52.

Pursuant to notice duly issued, the Department conducted public and evidentiary hearings at the Department’s offices on June 26, 2001. In support of its petition, the Company offered the testimony of Cheryl Yager, assistant treasurer for Southern Union. The evidentiary record consists of 22 exhibits and seven responses to record requests. On July 2, 2001, the Company submitted a brief in support of its petition. The Attorney General did not file a brief.

## II. DESCRIPTION OF THE COMPANY’S PROPOSAL

Southern Union proposes to issue and distribute up to 2.7 million shares of common stock as a dividend payment to the Company’s equity shareholders (Exh. SU-1, at 3). The Company asserts that the proposed distribution constitutes a five percent common stock dividend to shareholders, based on approximately 50,982,000 shares outstanding as of March 31, 2001 (id.).<sup>2</sup>

---

<sup>1</sup> On July 20, 2001, the Governor signed St. 2001, c. 44 amending G.L.c. 164, § 11 to authorize the Department to review and approve of stock issuances intended for the purpose of issuing stock and scrip dividends, with an emergency preamble allowing the act to take effect immediately.

<sup>2</sup> Southern Union stated that it will certify the exact number of shares issued as part of a compliance filing (Exh. SU-1, at 4).

The Company explained that following a corporate reorganization in 1994, it adopted a policy of issuing a five percent stock dividend (Company Brief at 4, citing Exh. SU-1, at 4; Tr. at 64).<sup>3</sup> In accordance with the Company's by-laws, the Board of Directors meets annually to declare a dividend as a percentage of outstanding shares of stock (Exh. SU-1, at 4).

Simultaneously, the Board sets a record and payment date and authorizes the issuance of shares to accomplish the stock dividend (id.). The stock dividend is announced to shareholders on the declaration date and is paid to all holders of Southern Union stock, including stock held in trust, as of the record date (id.; RR-DTE-5).<sup>4</sup> Because of the previous statutory prohibition to issue stock dividends, the Company's Board of Directors has not yet authorized the issuance of the necessary shares (id. at 3). Southern Union intends to certify to the Department that its Board of Directors has authorized the stock issuance, upon the Department's approval (id.).

For those shareholders who wish to receive a cash dividend in lieu of a stock dividend, the Company offers a Stock Dividend Sale Plan (the "Sale Plan"), which provides eligible common stockholders the opportunity to sell those shares that they receive as stock dividends (id. at 8; Exh. SU-18; Tr. at 31-38). The Company stated that the shares are sold on the open market over a period of several weeks, so as not to adversely affect the market for Southern Union's stock (id. at 31-32). The Company noted that shareholders participating in the Sale Plan are not charged for this service, and receive payment for their shares based on the average

---

<sup>3</sup> By way of illustration, a stockholder owning 100 common shares of Southern Union would receive, in lieu of a cash dividend, an additional five shares (Tr. at 28-29).

<sup>4</sup> The payment date generally follows the record date by 10 days to two weeks (Exh. SU-1, at 4).

price obtained for the aggregated shares over the allotted time period (Exh. SU-1, at 8; Tr. at 37-38).

Southern Union contends that the issuance of a stock dividend is important for two reasons. First, the Company states that the payment of a dividend in stock rather than cash allows Southern Union to use its retained earnings to finance infrastructure investments and enhanced customer service, which reduces the amount of short-term debt used by the Company (Company Brief at 10, citing Exhs. SU-1, at 7-8; SU-22; Tr. at 80-82). The Company analogizes its stock dividend program to dividend reinvestment programs (“DRPs”) offered by other utilities, which have been approved by the Department as a means to provide a continuous infusion of equity capital on a cost-effective basis (Company Brief at 11-12, citing Colonial Gas Company, D.P.U./D.T.E. 97-83, at 2 (1997)). Southern Union argues that stock dividends are more cost effective than DRPs because shareholders are able to increase their investment in the Company without incurring the tax liability of a cash dividend. (Company Brief at 11).

Second, the Company states that the payment of a stock dividend increases the number of shares that are available to be traded in the marketplace, which in turn, increases the liquidity in the Company’s stock (id. at 13, citing Exh. SU-1, at 7). Southern Union maintains that the Department has long supported efforts to increase the marketability of a utility’s stock, as a means of increasing investment and facilitate future financings at a lower cost, thereby benefitting ratepayers (Company Brief at 13, citing Fall River Gas Company, D.P.U. 93-147/172, at 7-8 (1993); Colonial Gas Company, D.P.U. 92-106, at 6-7 (1992); Fall River Gas Company, D.P.U. 87-160/87-193, at 3-5 (1987)). The Company argues that its stock dividend program has enhanced the liquidity of its stock, without adversely affecting

either the per-share value or total value of Southern Union's shareholders (Company Brief at 14, citing Exh. SU-1, at 9; SU-3; Tr. at 75).

### III. CAPITAL STRUCTURE OF THE COMPANY

As of March 31, 2001, the Company's utility plant (including \$27,158,000 in construction work in progress ("CWIP")) was \$2,205,321,000 (Exh. SU-4 (Rev.)). After removing \$758,717,000 in accumulated depreciation, the Company reported a net utility plant of \$1,446,604,000 (id.). In addition, the Company had \$41,639,000 of gas inventories and \$733,921,000 in acquisition premiums on its books (id.). Thus, as of March 31, 2001 the company had a net utility plant and gas inventory balance of \$2,222,164,000 (id.).

As of March 31, 2001, Southern Union reported a total capitalization of \$2,227,454,000, consisting of: (1) \$1,374,036,000 in long-term debt and capital-lease obligations (including the outstanding balance of a 364-day term loan and the pending \$400 million issuance of long-term debt that had been approved by the Department in Southern Union Company, D.T.E. 01-32 (2001)); (2) \$100,000,000 in preferred stock; and (3) \$753,418,000 in common equity (Exh. SU-4 (Rev.)). The Company's common equity balance included \$46,150,000 in retained earnings, which the Company intends to reduce by the amount of the stock dividend, with corresponding increases to the common stock and premium accounts (Exhs. SU-3; SU-4 (Rev.); SU-15).

The Company proposed a number of adjustments to these capitalization and net utility plant balances (Exhs. SU-1, at 11-12; SU-4 (Rev.)). First, the Company stated that it reduced its long-term debt and capital lease obligations by \$123,000,000 to remove the 364-day term loan, which the Company considers to be a short-term obligation for purposes of G.L. c. 164,

§ 14 (Exhs. SU-1, at 14; SU-4 (Rev.)).<sup>5</sup> Second, the Company excluded \$50,833,000 (\$76,016,000 in plant less \$25,133,000 in accumulated depreciation) from net plant in service associated with unregulated operations, with a corresponding reduction of \$50,833,000 to total capitalization, based on a pro rata reduction of \$30,614,000 in long term debt, \$2,375,000 in preferred stock, and \$17,894,000 in premiums on common stock (Exhs. SU-1, at 14-15; SU-4 (Rev.)).<sup>6</sup> Third, the Company explained that it excluded \$733,921,000 associated with acquisition premiums representing the excess of the purchase price over book value of several natural gas utilities acquired in recent years (Exhs. SU-1, at 16; SU-4 (Rev.); SU-5, at 22-23). The Company stated that a corresponding reduction of \$733,921,000 was made to its total capitalization, based on a pro rata reduction of \$441,573,000 in long-term debt, \$34,256,000 in preferred stock, and \$258,092,000 in premiums on common stock (Exhs. SU-1, at 16-17; SU-4 (Rev.)).<sup>7</sup> Fourth, the Company noted that it reduced its common equity by \$54,940,000 to eliminate net gains from changes in the market value of investment securities held by a subsidiary of the Company (Exhs. SU-1, at 17-18; SU-4 (Rev.)). Fifth, the Company stated that it excluded from capitalization \$46,150,000 in retained earnings (Exh. SU-1, at 18; SU-4 (Rev.)). Finally, the Company explained that it eliminated \$27,158,000 in CWIP from its plant investment accounts, along with \$14,806,000 in gas inventories so that only gas held by

---

<sup>5</sup> As of the date of the evidentiary hearing, the total outstanding balance of the 364-day term loan had declined to approximately \$85 million (Exh. SU-4 (Rev.); Tr. at 21).

<sup>6</sup> The Company's unregulated operations had been supported over the years through a combination of debt and equity (Exh. SU-1, at 15).

<sup>7</sup> The Company stated that it has financed its acquisitions over the years through a combination of debt and equity, and cannot directly attribute the acquired plant to specific capital items (Exh. SU-1, at 17).

Southern Union's regulated divisions were included in the total inventory balance (Exhs. SU-1, at 18; SU-4 (Rev.)). Based on these adjustments, the Company concluded that the excess of utility plant over capitalization amounted to \$130,686,000 (\$1,395,396,000 minus \$1,218,560,000) (Exh. SU-1, at 12).

#### IV. STANDARD OF REVIEW

In order for the Department to approve the issuance of stocks, bonds, coupon notes, or other types of long-term indebtedness<sup>8</sup> by an electric or gas company, the Department must determine that the proposed issuance meets two tests. First, the Department must assess whether the proposed issuance is reasonably necessary to accomplish some legitimate purpose in meeting a company's service obligations, pursuant to G.L. c. 164, § 14. Fitchburg Gas & Electric Light Company v. Department of Public Utilities, 395 Mass. 836, 842 (1985) ("Fitchburg II") citing Fitchburg Gas & Electric Light Company v. Department of Public Utilities, 394 Mass. 671, 678 (1985) ("Fitchburg I"). Second, the Department must determine whether the Company has met the net plant test.<sup>9</sup> Colonial Gas Company, D.P.U. 84-96 (1984).

The Supreme Judicial Court has found that, for the purposes of G.L. c. 164, § 14, "reasonably necessary" means "reasonably necessary for the accomplishment of some purpose having to do with the obligations of the company to the public and its ability to carry out those obligations with the greatest possible efficiency." Fitchburg II at 836, citing Lowell Gas Light Company v. Department of Public Utilities, 319 Mass. 46, 52 (1946). In cases where no issue

---

<sup>8</sup> Long-term refers to periods of more than one year after the date of issuance.  
G.L. c. 164, § 14.

<sup>9</sup> The net plant test is derived from G.L. c. 164, § 16.

has been raised about the reasonableness of management decisions regarding the requested financing, the Department limits its Section 14 review to a determination of reasonableness of the Company's proposed use of the proceeds of a stock issuance. Canal Electric Company, et al., D.P.U. 84-152, at 20 (1984); see, e.g., Colonial Gas Company, D.P.U. 90-50, at 6 (1990). The Fitchburg I and II and Lowell Gas cases also established that the burden of proving that an issuance is reasonably necessary rests with the company proposing the issuance, and that the Department's authority to review a proposed issuance "is not limited to a 'perfunctory review.' " Fitchburg I at 678; Fitchburg II at 841, citing Lowell Gas at 52.

Regarding the net plant test, a company is required to present evidence that its net utility plant (original cost of capitalizable plant, less accumulated depreciation) equals or exceeds its total capitalization (the sum of its long-term debt and its preferred and common stock outstanding) and will continue to do so following the proposed issuance. Colonial Gas Company, D.P.U. 84-96, at 5 (1984).

Where issues concerning the prudence of the Company's capital financing have not been raised or adjudicated in a proceeding, the Department's decision in such a case does not represent a determination that any specific project is economically beneficial to a company or to its customers. In such circumstances, the Department's determination in its Order may not in any way be construed as ruling on the appropriate ratemaking treatment to be accorded any costs associated with the proposed financing. See, e.g., Boston Gas Company, D.P.U. 95-66, at 7 (1995).

As amended by the General Court, G.L. c. 164, § 11 requires Department approval as a condition for issuance of stock for the purpose of scrip or stock dividends. For the following reasons, the Department has determined that the standard of review to be applied when



investigating the appropriateness of the issuance of stock will be the same standard of review used for financing petitions made under G.L. c. 164, § 14. Whether the Company issues cash dividends pursuant to G.L. c. 164 § 14 or declares stock dividends pursuant to G.L. c. 164, § 11, the effect is the same, in that the Company's common stock account increases. Under principles of statutory construction, statutes addressing the same subject matter are ordinarily construed to be consistent with one another. 2B Singer, Sutherland Statutory Construction § 51.02, at 189 (6<sup>th</sup> ed. 2000). See also Green v. Wyman-Gordon Co., 422 Mass. 551, 554 (1996); St. Germaine v. Pendergast, 411 Mass. 615, 626 (1992). Applying this principle to the instant matter, the Department has determined that petitions filed under G.L. c. 164 § 11 will be approved if the proposed issuance is reasonably necessary to accomplish some legitimate purpose in meeting a company's service obligations, pursuant to G.L. c. 164, § 14, and the Company has met the net plant test, derived from G.L. c. 164, § 16.

## V. ANALYSIS AND FINDINGS

### A. Issuance and Distribution of Common Stock Dividends

The Company has stated that its proposal to issue and distribute up to 2.7 million shares of a common stock dividend would provide it with a cost-effective means of securing equity capital to fund additions, extensions and improvements to the Company's utility plant and property. Moreover, the Company has testified that these additions, extensions and improvements would assist the Company in meeting its utility service obligations.

The Department has found previously that issuing stock for the purposes of acquiring and maintaining equity and increasing the liquidity and marketability of a company's stock is a "legitimate utility purpose" as contemplated by G.L. c. 164, § 14. See Fall River Gas Company, D.P.U. 93-147/172, at 7 (1993); Colonial Gas Company, D.P.U. 91-130, at 4

(1991). Accordingly, the Department finds that the proposed issuance is reasonably necessary to accomplish a legitimate purpose in meeting the Company's service obligations in accordance with G.L. c. 164, § 14.

B. Net Plant Test

In regard to the net plant test, the Department requires companies to demonstrate that their net utility plant equals or exceeds their total capitalization pursuant to G.L. c. 164, § 16 Colonial Gas Company, D.P.U. 84-96, at 5 (1984). As noted above, Southern Union has proposed a number of adjustments to its actual capital structure. Adjustments that the Company made excluding CWIP and retained earnings are consistent with Department precedent. New England Power Company, D.P.U. 92-189, at 7 (1992); Colonial Gas Company, D.P.U. 84-96, at 8 (1984). Accordingly, the Department finds that Southern Union's adjustments for CWIP and retained earnings are appropriate.

Concerning the proposed adjustment for the 364-day term loan, the Department notes that G.L. c. 164, § 14 defines long-term debt issuances as instruments with a maturity date of more than one year. As this loan is for less than one year, by definition, it is a short term debt. The Department has found that excluding short-term debt from capitalization is appropriate. Colonial Gas Company, D.P.U. 1247-A, at 7 n.2 (1982). Accordingly, the Department finds that the Company appropriately excluded the 364-day term loan from capitalization.

The Company has proposed excluding capital for unregulated operations. The Department has found previously that these costs of unregulated operations, including their capital costs, should be excluded from capitalization. D.T.E. 01-32, at 10-11. Accordingly,

the Department finds that the Company has appropriately excluded from its capital structure the capital used to finance unregulated operations.<sup>10</sup>

Similarly, the Company's proposed adjustment for acquisition premiums is appropriate, given that acquisition premiums, or goodwill, is intangible and as such, should be excluded as a component in a utility's capitalization for purposes of G.L. c. 164, § 16. D.T.E. 01-32, at 11; New England Power Company, D.T.E. 00-53, at 8-9 (2000). Accordingly, the Department finds that the Company appropriately excluded acquisition premiums from its capital structure.

The record demonstrates that, with the issuance and distribution of 2.7 million shares of common stock, the Company's total capital stock and long-term debt will not exceed the Company's net utility plant following the issuance and distribution of the common stock.<sup>11</sup> The procedures for issuance of dividends in the form of stock, see supra at 2-3, appear to offer sufficient safeguards and transparency to shareholders regarding their investments and to ratepayers regarding the continued operational soundness of the Company. Accordingly, the Department finds that the Company's issuance of no more than 2.7 million shares common stock meets the net plant test as provided in G.L. c. 164, § 16.

---

<sup>10</sup> The precise allocation of the Company's capitalization reductions associated with unregulated operations is best determined in the context of a rate proceeding brought under G.L. c. 164, § 94.

<sup>11</sup> Although Southern Union's total plant investment in Massachusetts is less than the amount of the financing sought, the Company's debt and equity financings are not specifically attributable to any particular jurisdiction (Exh. SU-1, at 17). Moreover, the Electric Restructuring Act of 1997 revised the definition of "gas company" to include non-Massachusetts corporations operating gas utilities within the Commonwealth. St. 1997, c. 164, § 189. Thus, the Company's combined operations are subject to the jurisdiction of the Department and the provisions of G.L. c. 164, § 14. Southern Union/Fall River Gas Company, D.T.E. 00-25, at 27 (2000); Southern Union/North Attleboro Gas Company, D.T.E. 00-26, at 26 (2000).

Issues concerning the prudence of the Company's capital financing have not been raised in this proceeding and the Department's decision in this case does not represent a determination that any project is economically beneficial to the Company or its customers. The Department's determination in this Order is not in any way to be construed as a ruling relative to the appropriate ratemaking to be accorded any costs associated with the proposed financing. A determination as to the appropriate ratemaking treatment to be accorded to common stock issued for the purposes of stock or scrip dividends requires a full examination of Southern Union's capital structure and cost components, which is best made in the context of a rate proceeding under G.L. c. 164, § 94. At that time, the Company would have the opportunity to present evidence to support its claims that its stock dividend program produces a lower overall cost of capital.

VI. ORDER

Accordingly, after due notice, hearing, and consideration, the Department hereby:

VOTES: That the issuance and distribution by Southern Union Company of no more than 2.7 million shares of common stock as a dividend payment to the Company's equity shareholders, is reasonably necessary for the purposes for which such issuance and sale has been authorized, pursuant to G.L. c. 164, § 14; and

VOTES: That the issuance and distribution by Southern Union Company of no more than 2.7 million shares of common stock as a dividend payment is in accordance with G.L. c. 164, § 16 in that the fair structural value of the Company's property, plant and equipment and the fair value of the gas inventories held by the Company, will exceed its outstanding stock and long-term debt; and

VOTES: That the issuance and distribution by Southern Union Company of no more than 2.7 million shares of common stock is approved and authorized in accordance with G. L. c. 164 § 11, that allows for the distribution of a stock dividend after approval and authorization from the Department; and

VOTES: That the issuance and distribution by Southern Union Company of no more than 2.7 million shares of common stock is approved and authorized in the Company's certification of a vote by the Board of Directors to authorize the stock issuance; and it is

ORDERED: That the Department approves and authorizes the issuance and distribution by Southern Union Company, in conformity with all the provisions of law relating thereto, of up to 2.7 million shares; and it is

FURTHER ORDERED: That Southern Union Company be authorized to issue and distribute a stock dividend; and it is

FURTHER ORDERED: That the Secretary of the Department shall within three days of the issuance of this Order cause a certified copy of it to be filed with the Secretary of State of the Commonwealth.

By Order of the Department

---

James Connelly, Chairman

---

W. Robert Keating, Commissioner

---

Paul B. Vasington, Commissioner

---

Eugene J. Sullivan, Jr., Commissioner

---

Deirdre K. Manning, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such further time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Acts of 1971).